NOTE BAN — A YEAR LATER


CASH OUT
HENCE
NO
EXCHANGE

ONE YEAR OF DEMONETISATION

In a decision that has few parallels in India's economic history, on November 8th last year, Prime Minister Narendra Modi announced the withdrawal of legal tender status to Rs 500 and Rs 1000 notes.

The move which effectively drained out 86 per cent of the currency in circulation, caused massive disruption to economic activity. As a consequence, GDP growth slumped to a low of 6.1 per cent in the fourth quarter of FY17.

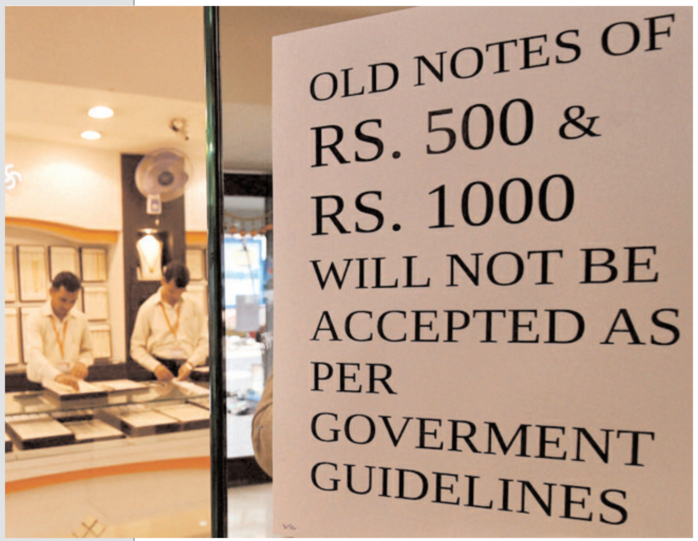
In subsequent months, while the process of remonetisation had gathered steam, economic activity was again disrupted as companies prepared to shift to the good and service tax (GST) regime.

As the one-year anniversary of demonetization approaches, Business Standard takes a look back at India's tumultuous year.

Till now the entire process leading up to that fateful day has been shrouded in secrecy.

Now, on the one- year anniversary of the announcement, Business Standard pieces together sequence of events leading up to that day, with details of the discussions that took place in the government as well as the officials involved in the process.

Looking back, a rather peculiar trend in the months that followed was the resilience of agriculture. While headline growth slumped in the quarter that followed, surprisingly agricultural production held up. But the effects of the decision reverberated across other parts of the economy.



Sensing a sharp downturn, markets tanked in the days after the announcement. The BSE Sensex fell by seven per cent within a fortnight of the announcement, with several consumer oriented and real estate companies crashing by more than 50 per cent.

Surprisingly, the market downturn was short lived. With households pouring money into mutual funds, domestic players stepped up. The market stabilised, turning the corner towards the end of December.

While markets have since then moved from strength to strength, the quarterly results of companies paint a dismal picture. Particularly hit were the small and medium enterprises. To gauge how they have fared over the past year, Business Standard spoke to small businesses in the cities of Kanpur, Tirupur, Bhiwandi and Ludhiana.

GROWTH FALTERED AFTER DEMONETISATION

It is the informal sector that has been more adversely affected. The impact of the note ban exercise on it cannot be quantified in the absence of data

DALIP KUMAR

ISHAN BAKSHI & SANJEEB MUKHERJEE

It was a decision with few parallels in India's economic history. On November 8, 2016, in an address to the nation, Prime Minister Narendra Modi announced the withdrawal of legal tender status to ₹500 and ₹1,000 notes.

In a nation that transacts primarily in cash, the decision withdrawing 86 per cent of the currency in circulation wreaked havoc, disrupting economic activity.

It also effectively shattered the hopes of a consumption-oriented recovery, which many economists had predicted would begin towards the second half of FY17, thanks in part to a good monsoon and proceeds from the Seventh Pay Commission.

The headline growth numbers held up in the third quarter of FY17, but dipped thereafter to 6.1 per cent in the fourth quarter. Excluding public spending and agriculture, growth slowed to a mere 3.8 per cent in Q4FY17 — revealing the extent of the slowdown in the formal sector.

But these numbers don't reveal the true extent of the slowdown.

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"The quarterly GDP numbers are largely based on the formal sector data, and as such do not reveal the true extent of the slowdown in the informal economy, which was more badly hit," says Pronab Sen, former chief statistician of India.

Many feared that the cash crunch in the economy would badly sting India's cash-intensive rural economy.

While the subsequent production and acreage data showed that sowing was better than in previous years and rabi production in FY17 touched a high of 137.16 million tonnes, the events that unfolded in the months thereafter lead many to argue that demonetisation had indeed broken the back of the rural economy.

The slowdown in economic activities and the massive drop in household demand led to a crash in prices. Retail and wholesale prices of commodities such as pulses, onion, vegetables, and oilseeds dropped well below their minimum support prices (MSP). As a consequence, GVA by agriculture and allied activities grew by a mere 0.3 per cent (current prices) in Q1FY18.

"Demonetisation and its aftermath halted whatever little recovery the rural sector was witnessing post two back-to-back droughts of 2014 and 2015," says Himanshu, associate professor at Jawaharlal Nehru University.

"Prior to demonetisation, these sectors (rural non-farm sectors) were facing a stress, but 2016 onwards, things were getting better as the monsoon was good, but the benefits of a good monsoon were denied to the rural sector due to demonetisation. Further, rural wages, which had started showing a rising trend since July 2016, continued till January 2017, but after that they have slowed as the impact of demonetisation set in," he adds.

Other experts concur.

"Agriculture was badly hit and this had knock-down effects on the non-agricultural unorganised sector, which in turn impacts the organised sector," says Sen. "Also in the informal sector, financing typically flows from informal sources of credit. My sense is that demonetisation has broken those chains," he adds.

But in the absence of data it is difficult to know for sure.

In the midst of all this, the Reserve Bank of India released its annual report for 2016-17, revealing that of the ₹15.76 lakh crore of the currency that was withdrawn, ₹15.28 lakh crore had been deposited back — dealing a big blow to expectations of lakhs of crores of black money not being returned back into the system.

While there was initial scepticism over the pace of remonetisation, once it gathered steam, economists expected the economy to bounce back in subsequent months. However, they were in for a rude shock.

As the deadline for shifting to the new indirect tax regime approached, firms cut back on production and resorted to destocking their inventory. As a result, GDP growth slumped to 5.7 per cent in the first quarter of FY18, with manufacturing growing at a minuscule 1.2 per cent.

While many are expecting growth to bounce back — a recent SBI research report pegs growth at 6 per cent in Q2FY18 — others are sceptical.

There are two contrary forces that are operating in tandem right now.

"One, the destocking we saw in Q1 is likely to reverse and companies increase production and build up their inventories; and second, the disruptive effects of the goods and service tax (GST) on the formal economy," says Sen. How they play out will determine whether growth will revive in the coming quarters or not.

NOTE BAN HAS BEEN LIFE BLOOD FOR A LISTLESS OPPOSITION

The year 2018 should be interesting as the Modi government tries to win back the confidence of the middle class before the Lok Sabha elections

ARCHIS MOHAN

At 5.30pm on Tuesday, November 8, 2016, the Reserve Bank of India approved demonetisation at its board meeting in Mumbai. A little later in New Delhi, Prime Minister Narendra Modi informed his Cabinet colleagues of the decision. If any of them had any misgivings, they thought fit to keep those to themselves. But a senior Cabinet minister, widely recognised as one of the performers in the Modi Cabinet and someone known to speak his mind, asked whether the Prime Minister and his team had weighed the pros and cons of scrapping 86 per cent of the currency overnight.

The minister, who would have to go nameless, got a forthright reply from Modi. "I have done all the research. If it fails, I am to blame," the PM said. If his ministers were gobsmacked, the PM left the Opposition leadership equally nonplussed after his famous address to the nation at 8 pm.

As the evening progressed, the Congress waited for senior leader P Chidambaram to prepare a critique. West Bengal Chief Minister Mamata Banerjee, who trusts her instincts like few others on the Indian political scene, conveyed her assessment to the leadership of her former party. Banerjee, who had quit the Congress to form the Trinamool Congress in 1997, wanted the Congress to take the lead in slamming the "anti-people" move. According to a Trinamool leader, she thought it was a defining moment in the life of the Modi government. Impatient at the delay from the Congress, Banerjee issued a series of tweets from 9.30 pm to criticise the move.

Exceptions like Bihar Chief Minister Nitish Kumar aside, demonetisation provided a lifeline to a listless Opposition. While the PM alleged that all who opposed the move were corrupt, the note ban brought a new synergy among the Opposition parties. The arch-rivals Samajwadi Party and Bahujan Samaj Party, Trinamool and the Left parties made a common cause to flay the move. For two years, the Opposition had waited for the people to get disillusioned with Modi's magic. Their brief moment had come in the early months of 2015, when they had put the government on the mat for its land acquisition Bill. The jibe that Modi's was a 'suit-boot *ki sarkar*', or a government of and for the moneybags, had hurt the government enough for it to rethink its promise of delivering reforms. The PM had quickly recovered lost ground, as his government unleashed its "*garib*

kalyan", or welfare of the poor, agenda.

In the weeks after demonetisation, the Centre changed the goalposts and issued nearly 150 notifications. The initial objective of the note ban was to end black money. Within weeks, the PM said the real aim was to encourage cashless transactions and digitisation. Businesses and traders suffered. Some shut down. There were also reports of people dying standing in queues. If Congress Vice-President Rahul Gandhi stood in an ATM queue in New Delhi to withdraw money, the PM's 96-year-old mother was wheel-chaired to a bank in her village to withdraw money.

The PM's personal credibility, however, remained intact. He led his party to a famous win in the Uttar Pradesh Assembly election in March. The BJP claimed the win was a referendum on demonetisation. The emphatic victory also gave Modi the confidence to go ahead with the rollout of the goods and services tax (GST) on July 1. The Congress and the rest of the Opposition have faulted the GST as "flawed". According to reports from across India's industrial hubs, the MSME (micro, small and medium enterprises) sector has suffered. The government has again needed to do much fine-tuning of the system, but even Sangh Parivar organisations working among the MSME sector and workers are upset.

Government and RBI data have also made it evident that demonetisation has failed to meet most of its stated objectives. The Opposition believes economic slowdown and joblessness are changing the narrative on the ground. Rahul Gandhi has termed it an 'MMD', or a 'Modi Made Disaster'. But the BJP leadership expects to ride out the crisis. The top BJP leadership is confident that the party will win the Himachal Pradesh and Gujarat assembly polls, and will showcase the victory as a referendum on the GST and its execution.

SOME GOVT AND RESERVE BANK DATA HAVE ALSO MADE IT EVIDENT THAT DEMONETISATION HAS FAILED TO MEET MOST OF ITS STATED OBJECTIVES

There are still 18 months to go for the 2019 Lok Sabha elections. Opposition parties say people are waking up to the view that the promised 'achche din', or better days, is illusory. It has also collectively decided to persist with questioning the government on economic issues, and not engage on emotive issues of "nationalism".

The year 2018 should be interesting as the Modi government tries to win back the confidence of the middle classes before the Lok Sabha elections. There are a string of Lok Sabha bypolls and assembly elections in Tripura, Meghalaya, Nagaland, Mizoram, Karnataka, Rajasthan, Madhya Pradesh, and Chhattisgarh, which would indicate the mood of the people in the run-up to the 2019 Lok Sabha polls.

THE DIGITAL ROLLER COASTER: FROM DIGITAL TO LESS CASH

For weeks after note ban, India was downloading e-wallet apps, applying for credit cards and buying PoS machines

KARAN CHOUDHURY & ABHISHEK WAGHMARE

A half-torn poster of Paytm Wallet with first four digits of Ashok Mondol's mobile phone pasted on the side of his grocery shop in Chittaranjan Park, a South Delhi residential colony, is the only evidence left of him ever accepting digital money. Till November last year, Mondol used his smartphone mostly to watch films. But, after note ban, for some period, it became the main tool that kept his shop afloat.

Thanks to his daughter, Mondol managed to get in touch with agents from Paytm, MobiKwik, Freecharge and Oxigen who taught him how to use their respective mobile wallets. "It became my shop's lifeline. I could finally run my business," he said. However his digital journey ended soon enough. "Cash came back to the market. Also mobile wallets have a limit to the money that can be transacted on the platform and they charge service fees, making it unviable in a low-margin business," he said.

The first thing that people read on the morning of November 9, 2016, after Prime Minister Narendra Modi left the country awestruck and shocked, were full-page jacket advertisements in leading dailies by mobile wallet major Paytm. Freecharge followed a day later. They thanked the PM for the revolutionary step. Digital money in the country had finally got the ultimate push, thanks to a little known word till then, demonetisation.

In the days and weeks following note ban, India was downloading mobile wallet applications, applying for credit cards, buying point of sale machines and finding the long forgotten online account PIN number in old files to make payments for anything and everything.

What the numbers say

During the subsequent months, six new mobile wallets were launched, Axis Bank bought Freecharge and Bajaj Finance took 11 per cent stake in Mobikwik for Rs 225 crore, both hoping to make their digital play stronger. The industry together put in close to a billion dollars to find, educate and add more users.

The government on its part tried everything to make India 'cash less'. However, realising that making people forget about cash was next to impossible, the government shifted to the 'less-cash' slogan. It has ever since pushed every type of digital method of money transfer in an effort to coax people to rely less on paper currency.

In the last one year, the government organised magnum opus events such as ‘Digi-Dhan Mela’ hosted by the PM, launched new digital ways of transaction including apps such as BHIM, Unstructured Supplementary Service Data (USSD), Bharat QR, Aadhaar Pay and even a television channel ‘DigiShala’ to educate people on the virtues of cashless transactions.

While the year-on-year growth in digital transactions--all modes of payment under payment system indicators in RBI database--spiked in the immediate months after November 2016, growth rate of both, value and volume of transactions, has gone back to pre-demonetisation levels. In select five modes of payment which the masses access — namely NEFT, IMPS, cheque payment, usage of debit cards at point-of-sale machines and prepaid payment instruments that include UPI and wallets like Freecharge and PayTM--registered growth in value and volume of transactions was higher, and has settled on a higher normal than pre-demonetisation level. In both cases, growth in digital transactions has, however, plateaued over the last few months.

Subdued growth in ATMs while improved growth in point-of-sale machines specifically point to a sustained shift from cash to less-cash. While growth in number of ATMs has reduced from 13 per cent a year before demonetisation to 3 per cent a year after it, growth in number of PoS machines has skyrocketed from 10 per cent to 97 per cent.

GST elbows out ‘less-cash’ initiative

On July 1, the government rolled out Goods and Services Tax (GST), the biggest indirect tax reform in the country. Since then, digitisation of cash has taken a back seat, experts believe.

“There were a series of things that happened late last year. A significant plan for digitisation, fresh set of PPI guidelines, Wattal Committee recommendations all led to the biggest shift in digitisation of money which resulted in a spike in digital transactions. But a lot more could have been done. After the government started struggling with the roll out of GST, the digital money initiative took somewhat of a back seat,” Prosanto Roy, vice-president, NASSCOM, and head internet, mobile, ecommerce and domestic market, said.

WHILE GROWTH IN THE NUMBER OF ATMs HAS REDUCED FROM 13% A YEAR BEFORE DEMONETISATION TO 3% A YEAR AFTER IT, GROWTH IN THE NUMBER OF PoS MACHINES HAS ZOOMED FROM 10% TO 97%

Safety concerns

The safety of digital transaction is another major reason which is causing a delay in more people adopting electronic payment methods. According to PwC India, the country has witnessed nine major cyber attacks of financial establishments in the last 12 months starting from WannaCry ransomware attack, hacks on financial services group Religare and malware attack on thousands of BSNL broadband modems to name a few.

“I think cyber security setup in India enjoys a large mindshare among the leaders but unfortunately not enough pocket share. Over the last year or so, we’ve seen some big hacks happening across sectors. We’ve also seen an increase in the regulatory interventions from RBI, IRDAI among others which is a welcome step. But there continues to be much left to do,” said Siddharth Vishwanath, partner, Cyber Security, PwC India.

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Experts also believe that while roll out of digital transaction methods has been faster, tools to protect them are still scarce.

“The IT Act 2000 did not have any parameters for cashless transaction, even rules for regulating digital payments is not in place. All this has made India one of the most fertile grounds for cyber crimes. Even the GST network which has faced a lot of criticism is at risk of hacks,” said Pavan Duggal, cyber law expert and Supreme Court advocate.

Industry stays bullish

In the weeks following demonetisation, mobile wallet major saw its user base go up from 125 million to 230 million. Others have similar stories to tell and numbers to prove that digital money is thriving.

“We have not seen any drop in the number of digital transaction, it has only gone up. People who used mobile wallets during demonetisation for the first time tasted blood and now we have 10 million small retailers online. Every other year we hear that wallets are dead, but is that really the case,” asks Upasana Taku, Co-Founder, MobiKwik. The government has not forgotten about the digital wallets and other methods of transaction, according to Taku. “We just got the new master guidelines, the initiatives by the government are still on track.”

Way forward

Industry experts believe that for digital and less-cash initiative to be a success story, the government needs to shift its focus. “The government needs to decrease friction in digital transactions. There should be parity in what one pays online and offline,” said Roy. The government should take all payments digitally, from fees and fines to even entry tickets to historical monuments. “Also, the Jan Dhan Yojana needs to be reviewed.”

DEMONETISATION SCARE SHORT-LIVED FOR STOCK MARKETS

After initial sell-off, it's been a one-way rally for equities after December-end

SAMIE MODAK

Prime Minister Narendra Modi's decision to ban high-value currency notes triggered a knee-jerk reaction in the stock market, with the benchmark Sensex and Nifty declining seven per cent within a fortnight of the announcement. Several stocks in the microfinance, real estate and other consumer-facing sectors crashed more than 50 per cent, creating panic and fear in the market. The sell-off was triggered by doomsday projections by economists that the note ban would lead to a prolonged weakness in the economy and further delay the earnings recovery cycle.

The Nifty, which was trading above the 8,500-mark before demonetisation, slumped to a seven-month low of 7,908 on December 26. The BSE Realty and BSE Consumer Durable indices dropped 17 per cent and 14 per cent, respectively, from November 8 to December 26. Blue-chip cement companies UltraTech Cement and Ambuja Cements and paint major Asian Paints saw their stock prices correct 20 per cent each on fears that the cash crunch would dampen demand. Non-banking finance company stocks such as Manappuram Finance, Bharat Financial Inclusion and real estate stocks such as Delta Corp plummeted over 40 per cent from their pre-demonetisation levels till December 26.

Fortunately for the Street, the pain lasted less than two months as the markets bottomed out on December 26 because of buying support from domestic institutional investors, mainly mutual funds (MFs).

MFs got a shot in the arm from demonetisation as surging bank deposits got channelled into their equity schemes. Taking advantage of the weakness, MFs stepped up buying, purchasing shares worth ₹24,000 crore in November and December even as overseas investors dumped shares worth more than ₹26,000 crore during the same period. The note ban announcement clashed with the global uncertainty created by Donald Trump's surprise victory in the US presidential elections.

While the jury was still out on the economic and earnings impact due to demonetisation, the stock markets shrugged all such worries and charted a sharp recovery. Foreign institutional investors (FIIs) joined the party from January-end amid a revival in global risk appetite. In February and March, FIIs invested ₹10,485 crore and ₹33,782 crore, respectively, in Indian stocks, lifting the Nifty by 15 per cent from its demonetisation lows.

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Globally, investors — who were initially apprehensive of Trump's protectionist stance — started lapping up risky assets on optimism that the US President would announce a cut in corporate tax and boost infrastructure spending.

Also, stability on the geopolitical front and the benign stance by global central banks provided ample liquidity for FIIs to invest in equity markets around the world, including India.

The 30-share Sensex, which had declined to 25,807 on December 26, for the first time closed above 30,000 on April 26, went on to climb to32,000 by end-July and breached the 33,000-mark in the last week of October.

A unique feature of this rally has been low volatility. The India VIX index, a gauge for market volatility, has averaged only 13 since the demonetisation lows of December 26.

Declining bank deposit rates and dimming assets of other asset classes such as real estate, accelerated flows into MFs. Since November 2016, equity MFs saw a massive ₹1.25 lakh crore of flows.

The huge FII buying seen during January-February subsided over the next few months and since August they turned into huge net-sellers. Since August, FIIs have pulled out ₹26,000 crore (over $4 billion) from the cash market. However, this failed to make too much of a dent on the Indian markets because of aggressive buying by domestic MFs, who were flush with investor flows.

Despite the rally, the fundamental concerns about the economy and corporate earnings continue to puzzle analysts. The 20 per cent gain made by benchmark indices since November 8 have been largely on the back of valuation expansion. The Indian markets currently trade at over 20 times its one-year forward earnings compared to the long-term average of 16 times.

Demonetisation, coupled with the introduction of the goods and services tax (GST), has deferred earnings recovery by at least three quarters. Analysts are hoping a sharp revival in corporate earnings from the December quarter onwards, albeit on the low base created by demonetisation.

THE BACKROOM STORY: HOW IT ALL PLAYED OUT

Preparations or discussions had begun within the government, more specifically in the PMO, almost a year before the announcement

SUBHOMOY BHATTACHARJEE

It was evening news time in television studios that Tuesday. In the state broadcaster Doordarshan's newsroom, a routine advisory had landed up from the government about a possible list of experts who could be called for their views on an expected news break.

Just a few hours earlier on November 8, 2016, Prime Minister Narendra Modi had met the chiefs of the army, air force and navy. Rumour mills were working full time by now and there were whispers about likely wars that the government could announce. The list of possible experts that arrived around 7.30 pm surprised everyone. There were no security or military experts. Instead, plenty of economists, within and outside the government, filled up the list. Half an hour later, the PM announced demonetisation, India's biggest ever monetary gambit.

There was also a Cabinet meeting in progress at 7, Lok Kalyan Marg. The items were fairly innocuous. Few except the secretaries concerned would remember them later. The government made no announcements on them the next day. One of the secretaries who was there with his minister was startled when he arrived home by 8 pm. "Look at the TV", his wife told him.

Some bureaucrats recalled that more than usual number of officers from the Cabinet Secretariat and the Prime Ministers' Office were milling about near the Cabinet rooms that day.

"Is something big about to be announced", queried one of the officers at the venue. There was no clear answer as no one seemed to be in the loop.

IS SOMETHING BIG ABOUT TO BE ANNOUNCED", QUERIED ONE OF THE OFFICERS AT THE VENUE. THERE WAS NO CLEAR ANSWER AS NO ONE SEEMED TO BE IN THE LOOP

Yet, it was almost a year before the actual announcement that preparations or discussions had begun within the government, more specifically in the Prime Minister's Office, about demonetisation. Those meetings were attended by some of the top officers from the finance ministry, cabinet secretariat and PMO. As RBI's then Governor Raghuram Rajan says in his book 'I do what I have to do', he was asked for his opinion in February 2016 at one of those meetings, just days before the Budget was to be presented in Parliament by Finance Minister Arun Jaitley. "I was then asked to prepare a note, which the RBI put together and handed to the government. It outlined the potential costs and benefits of demonetisation".

There were preliminary discussions before that eventful meeting but it was post Budget that the process began in earnest.

As Rajan adds, the deputy governor of RBI in charge of currency attended the subsequent meetings through the summer. By September, Rajan had quit RBI but the core group remained unchanged. Even within the core group, members were not always aware of each detail—Rajan's note was not mentioned in the meetings.

One of the key queries asked in the run up to demonetisation was whether the Reserve Bank of India's currency department could stock up additional currencies of ₹100 and ₹50 to flood the economy once the high-value notes were

BEFORE THE PM WENT LIVE ON DOORDARSHAN, THE DECISION HAD TO BE OKAYED BY AT LEAST ONE CABINET BODY. THE OBVIOUS CHOICE WAS THE CABINET COMMITTEE ON SECURITY. WITHIN WHICH THE FINANCE MINISTER AND THE HOME MINISTER WERE ALREADY ON BOARD ABOUT THE EXERCISE THROUGH THE YEAR

withdrawn suddenly. It was given up for logistical reasons.

The officers were clear that such an exercise would not pass unnoticed. The annual requirement for currency notes was set at the beginning of the year and any massive ramp up would be clearly noticeable to the staff. It would hold true whether the printing went on at the modernised and automated presses at Mysuru and Salboni or the much older ones at Nashik and Dewas.

The other key decision to make was the date of the announcement. "There was a window of opportunity just after Diwali for about a fortnight", said an officer who had watched the developments from close quarters. Despite being a busy season, the rush of pre-Diwali consumption would be over. However, the final decision for November 8 was decided upon, just weeks before the D-Day. There was a proposal to push the date to a subsequent Friday to give banks the weekend to prepare themselves for the rush. But despite the secrecy, rumours were beginning to swish around about a possible demonetisation. For instance, in the monsoon session of Parliament, close to 8 per cent of Rajya Sabha questions to the finance ministry was on black money. MPs asked more questions on it than about public sector banks. Something was afoot.

Just about 24 hours before 8th, the core group informed the chiefs of the security agencies including the Intelligence Bureau. Officers in those agencies lower down the line were informed just hours before, on that Tuesday. It was a calculated risk which was apparently debated within the core group and had been decided accordingly. Now there was no rolling back of the process. India had never been here before.

Before the PM went live on Doordarshan, the decision had to be okayed by at least one cabinet body. The obvious choice was the Cabinet Committee on Security within which the Finance Minister and the Home Minister were already on board about the exercise through the year. The Defence and Foreign ministers too needed to be briefed about the announcements, especially as there would be questions from the foreign capitals, about the move. In Mumbai, a similar exercise had begun in RBI. Though Rajan's successor Urjit Patel was already in Delhi, bank chiefs were asked to come over to the RBI headquarters for a meeting. A video conferencing meeting should have given them some clue, but surprisingly none of the chiefs seemed to have caught what was coming.

As the cameras began rolling at the Prime Minister's residence, both revenue secretary Hasmukh Adhia and economic affairs secretary Shaktikanta Das, who were part of the core group, were back at their offices. "I called the joint secretaries to my room, switched on the television and sat down to hear the Prime Minister", one of them said. With the Prime Minister's voice filling up the room, the officers were handed out their assigned duties. Calls to the police chiefs and chief secretaries in state governments began to go out. It was going to be a long night.

NOTE BAN LOGIC: CLEAN MONEY, RETURN OF THE RAID BRIGADE

The tax department has been creating psychological profiles of select people on its radar since demonetisation

ILLUSTRATIONS : AJAY MOHANTY

SAI MANISH

One of the first justifications given by Prime Minister Narendra Modi for knocking 86 per cent of the Indian currency out of circulation last year was curbing the dominance of black or unaccounted money in the economy. While the return of a significant amount of money into the banking system might have raised doubts over the black money motive, there seems to be growing enthusiasm among income-tax investigators to raid those suspected of possessing unaccounted money. However, the rise in the number of raids hasn't seen a corresponding increase in the money seized.

Tax investigators searched over a thousand so-called 'groups' in 2016-17 and managed to seize about ₹1 crore on an average from each of them. The number of groups raided rose almost 84 per cent since the Modi government assumed power in 2014. During the raids, almost ₹19,000 crore was either detected by tax investigators or admitted by those being raided during questioning.

There also seems to have been an enhanced surveillance push and tax crackdown since demonetisation. According to the Ministry of Finance, 56 people have been put under Central Bureau of Investigation or Enforcement Department probe. More than 6,400 people who were surveyed admitted to

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holding unaccounted wealth worth about ₹7,000 crore. Half a million cases have been earmarked for further verification by the tax department. About 850,000 people have been classified as high-risk individuals.

All of this has been carried out under the ambit of 'Operation Clean Money' launched in December last year. Two yet unknown companies were given the contract in March 2017 to mine millions of bits of information on the nature of deposits made after the currency ban. What gives this a tinge of surveillance is the fact that the job of these two contractors wasn't just limited to analysing data regarding deposits of currency into bank accounts from the morning of November

9, 2016. One of the tasks set forth in the request for proposal was to "conduct fund tracking on transactional data for high-risk cases if no response was received from the depositor."

What looks intriguing is the fact that the two contractors were mandated to submit, among other things, a psychological profile of all those who were sent communications by the tax department. According to the department, almost 1.8 million people across India were asked to explain the source of their deposits following the currency ban. These people were to be ranked into four categories on a compliance behaviour scale – disengaged, resisters, triers and supporters. 'Disengaged' people were defined as those "who have decided not to comply. People with this attitude either deliberately evade their responsibility or choose to opt out." 'Resisters' were those "who don't want to comply but who will if they can be persuaded that their concerns are being addressed." The 'triers' were those "who are willing to comply but have difficulty in doing so, and don't always succeed." On the other hand, 'supporters' were defined as those who "demonstrate a willingness to do the right thing and make a conscious commitment to support the system."

These people were to be further plotted on a knowledge scale — a person with low 'awareness level' was classified as one having "less knowledge of tax laws". In addition, an indicative report of the authenticity of contact details provided by the people to whom communications were sent was also to be prepared. It is unclear how the tax department or the contractors are undertaking the process of tracking down a person's contact details without a helping hand from UIDAI.

This psychological profiling has been supplemented with a complete money profile of the person, including his past transactions. Each economic profile of the individual in the form of a report is being assigned a serial number. These have details such as his mobile number, residential address, home bank branch information, details of the branch in which the money was deposited, among other things.

The finger of suspicion on an individual has been raised after validating two other aspects of his financial behaviour. One of them was to get information about the amount of money credited into his account between April 1 and November 8, 2016. This was provided by banks from account statements issued to their customers. The contractors were expected to requisition past transaction data from banks, especially with regard to people who did not respond to communications from income-tax authorities. This was to be compared with the amount of money credited into the same account by the same person from November 9 to December 30, 2016. According to the departments' proposal, the people who were to be profiled would be those who deposited more than ₹12.5 lakh in a current account between November 8 and December 30, 2016. For those with other forms of bank accounts, such as a savings bank account, the limit was fixed at ₹2.5 lakh.

Tax surveillance currently happens most of the time in India under various rules. The Financial Intelligence Unit (FIU), which operates under the Ministry of Finance, receives Suspicious Transaction Reports (STRs) in addition to Cash Transaction Reports (CTRs) in cases where more than ₹10 lakh has been transacted every month in an account. But these reports do not contain psychological profiling of individuals as is being conducted under 'Operation Clean Money.'

Such profiling is consistent with the Modi government's intentions to empower tax investigators. In his 2017-18 budget speech, Finance Minister Arun Jaitley had proposed to "authorise the joint director, deputy director or the assistant director of income-tax to call for information for the purpose of any enquiry without seeking approval of the higher authority."

ACCORDING TO THE DEPARTMENT, ALMOST 1.8 MILLION PEOPLE ACROSS INDIA WERE ASKED TO EXPLAIN THE SOURCE OF THEIR DEPOSITS

The nature of such profiling also means that tax authorities would not only have a list of tax offenders, but also a list of 'high-risk' people who are not tax offenders but could turn into tax offenders in the future. This profiling push can partly be explained by the fact that demonetisation hasn't accelerated the increase in the tax base of the country.

According to the Central Board of Direct Taxes, in the November-March period of 2015-16, almost 40 million more people filed income-tax returns over the same period the previous year. In 2016-17, after demonetisation, the increase in the number of people who filed tax returns in the same period was around 3.3 million.

With the income-tax department armed with financial and psychological profiles of select individuals, the government could well be banking on a never tested data mining-fuelled brand of tax surveillance that aims to get more Indians to pay tax.

HOW THE MODI GOVT JUGGLED & STRUGGLED WITH JUSTIFICATIONS

The PM and his men have been clutching at straws the past one year to explain why the note ban was imposed on the citizenry

SHIVANSH JAUHRI

Narendra Modi has always been a prime minister in a hurry. In his zeal to fulfil his promise of transforming the Indian economy, he launched a slew of schemes such as Make in India, Start-up India and Jan Dhan, all within the very first year of coming to power. Even when he made what is possibly the biggest and most impactful economic announcement in independent India's history on November 8, 2016, he left very little space for the citizenry to respond. The PM's declaration that from the midnight of that day, ₹500 and ₹1,000 currency notes would no longer be legal tender, came late evening, much after normal banking hours, forcing people to queue up at petrol pumps, metro stations and other establishments that were still accepting the banned notes.

Over one year since the note ban was announced, the government has tried to justify its implementation by leaning on reasons as diverse as black money and terror funding, GST and realty prices to sell the diktat to the people. Here is a recap of such justifications:

November 8: Black money and fake currency

In his speech announcing the implementation of demonetisation, PM Modi had said, "For years, this country has felt that corruption, black money, and terrorism are festering sores, holding us back in the race towards development. ... To break the grip of corruption and black money, we have decided that the 500-rupee and 1,000-rupee currency notes currently in use will no longer be legal tender from midnight tonight, that is 8 November 2016." So here he listed corruption, black money, and terrorism as the key reasons for demonetisation. For the people, however, it was an ordeal standing in long queues to exchange notes just so they could meet their day-to-day expenses. "I've been standing here (outside a bank) since morning, I have money but cannot withdraw. How is this going to change things when we won't have money to buy food?" said a rickshaw puller standing in a queue on bone-chilling winter's day. However, according to RBI, banks got about ₹8.45 lakh crore worth of scrapped notes till November 28, 2016. There was also talk about India's economic security being jeopardised because of the growth of fake currency notes.

November 27: Digital/cashless economy

The demonetisation drive had some

DALIP KUMAR

DIGITAL WAS PROMOTED AND PoS MACHINES, SWIPE MACHINES, MOBILE ATMs AND SUCH LIKE WERE PROVIDED. DIGITAL TRANSACTIONS DID SHOOT UP ACCORDING TO A NITI AAYOG PRESS RELEASE WHICH SAID, "THERE HAS BEEN A PHENOMENAL 584% INCREASE (0.3 TO 4.5 MILLION) IN TRANSACTIONS MADE THROUGH THE UNIFIED PAYMENTS INTERFACE

immediate and devastating effects, with a spate of deaths being reported among people lined up in serpentine queues and a prolonged cash-crunch threatening the socio-economic situation in the country. The Prime Minister, in his 'Mann ki baat' edition of 27 November 2016, dwelt at length about demonetisation saying it would put an end to the corruption of the privileged -- the rich and the resourceful who had hitherto enough opportunities to siphon off money. He declared that this was a national fight against black money and corruption. However, Modi went on to say that this move was designed to take India towards a digital economy, a cashless economy. This, even as the citizenry was struggling with a severe paucity of liquidity (read currency). A news channel reported that most ATMs had run dry and the few that were functional were confronted with never-ending queues. One banker from Agra said RBI wasn't sending enough small currency notes and that the new ₹2,000 notes were not serving any purpose.

December: Cashless or less-cash

While the Prime Minister had stressed on cashless economy, Finance Minister ArunJaitley had, on several occasions,claimed demonetisationwas a drive aimed at achieving a 'less-cash' economy, as opposed to a cashless economy. While both the terms sound similar, there is a difference between the two. Following Modi religiously, a village in Dhasai in Maharashtra's Thane district, a predominantly tribal dwelling, became the state's first cashless rural habitat on December 1, 2016. However, not even a year down the line, the village started using cash again. In other parts of country too, digital was promoted and PoS (point-of-sale) machines, swipe machines, mobile ATMs and such like were provided. Digital transactions did shoot up according to a NITI Aayog press release which said, "There has been a phenomenal 584 per cent increase (0.3 to 4.5 million) in transactions made through the Unified Payments Interface (UPI) since demonetisation. In the same period, payments using Aadhaar have also seen an unprecedented jump of 1,352 per cent (0.7 to 2.7 million)."

December 27: Stop terror funding

The Reserve Bank of India was in no mood to be left behind in the race. RBI was probably quicker in changing norms for cash withdrawal and deposit than the government was, on doing flip-flops over demonetisation. The apex bank initially restricted ATM withdrawal to ₹2,500 a day per card and later increased it to ₹4,000 and ₹4,500. However, it did allow farmers to buy seeds using old currency notes. As the first deadline to deposit the banned notes — December 31, 2016 — approached, Modi once again changed his narrative on demonetisation, offering a rather unexpected reason for the drive. On December 27, 2016, while addressing a rally in Dehradun, he said demonetisation was done to put a stop on terror funding. "With just one move on November 8, the world of terrorism, drug mafia, human trafficking and fake note smuggling was destroyed. Most people are for honesty; it is just a handful who are trampling them. We have waged this war to empower those who are being trampled," he claimed. Deposits in Jan Dhan account reportedly doubled to Rs87,000 crore in 45 days post demonetisation.

January 11: Widen tax base

The deadline was extended and it was now Finance Minister ArunJaitley's turn to deliver his narrative. And yes, it was another economic reason for demonetisation. On January 11, 2017, he said the note ban was done to widen the tax base. "Targeted verification of suspect substantial deposits is likely to widen and deepen the tax base," he told the parliamentary panel. He went on to say that demonetisation would also foster a transparent economy and pave way for better economic growth. "Along with other measures for increasing transparency and strengthening enforcement, demonetisation will pave the way for sustainable faster economic growth," said Jaitley.

January 26: Transparent Economy

PHOTO: REUTERS

Demonstrators try to cross a police barricade during a protest against demonetisation organised by the Trinamool Congress

THE RESPONSE OF THE GOVERNMENT TO PUBLIC ANGER HAS ONLY FUELLED THE IMPRESSION THAT MODI AND HIS TEAM WERE THEMSELVES NOT VERY SURE ABOUT THE MOTIVES OF THE NOTE BAN

On the eve of Republic Day 2017, the then President Pranab Mukherjee hailed the government's demonetisation move and said it would lead to a transparent economy. "Demonetisation, while immobilising black money and fighting corruption, may have led to a temporary slowdown of economic activity. As more and more transactions become cashless, it will improve the transparency of the economy," he said in his address.

January 31: Realty prices are the devil
By January end, we had yet another reason for demonetisation. Chief Economic Advisor ArvindSubramaniam added real estate prices to the list of drivers. On January 31, 2017, he said, "You do see a blip in real estate prices, sales and launches and of course some of it may be adverse to the economy but in the long, some of that could be good because the aim of demonetisation is to bring down real estate prices. On the short-term effect on the real estate sector through December-end, the Economic Survey said, "Prices declined, as wealth fell while cash shortages impeded transactions".

July 23: Aid GST, grow GDP
When realty prices weren't turning out to be a big enough a reason, Jaitley brought GDP into the argument. Here's what he said in February: "Demonetisation was a bold and decisive strike in a series of measures to arrive at a bigger, cleaner and real GDP.... There is greater integration of informal economy taking place with formal economy that leads to larger and cleaner GDP, that was our objective behind the decision on demonetisation."

Jaitley also linked the note ban to the launch of GST. On July 23, he said, "Demonetisation coupled with the implementation of Goods and Services Tax regime will make generation of cash a lot more difficult, help towards the objective by creating greater compliance and increasing digitisation,"

Over the past one year, the Prime Minister and his men have been struggling to find a convincing reason to sell the demonetisation drive to the citizenry. Rapidly changing the 'triggers' every now and then has only given the impression that a desperate government has been clutching at straws to justify a move that seems to have caused more grief than good to the audience it was directed at. Worse, the response of the government to public anger has only fuelled the impression that Modi and his team were themselves not very sure about the motives of the note ban and whether or not its implementation achieved them.

DEMONETISATION IMPACT: MODI GOVT'S BHIM HAS HIT THE BULLS' EYE

But it will face its first big challenge from Google in the days to come, and will take a while before it can wean Indians off their love for cash

SAI MANISH

The government's BHIM (Bharat Interface for Money) application announced by Prime Minister Narendra Modi on December 31, 2016, has seen remarkable growth over the past few months. Named after Dalit icon Bhimrao Ambedkar, the digital payment application was also launched for non-smartphone users on his birth anniversary in April this year. During the first nine months of operation, BHIM has reported transactions worth more than ₹11,000 crore and now accounts for almost half of all United Payment Interface (UPI) transactions in the country.

National Payments Corporation of India figures show that in September this year, more than ₹2,400 crore worth of transactions were done on the BHIM platform. On an average, every transaction on BHIM was worth almost ₹3,000. These figures vindicate the Modi's government's resolve to transform India into a less-cash economy by introducing multiple digital platforms, with BHIM being one of them. With a transaction limit of ₹20,000 a day, the application was largely targeted at small and medium merchant establishments.

BHIM seems to have outdone most other non-cash based financial instruments that have gained traction among India's newly banked population since demonetisation. For instance, RuPay debit cards, which have been in use since 2012, clocked transactions amounting to ₹18,300 crore in the first half of 2017-18 at point-of-sale machines. In contrast, BHIM has recorded transactions worth ₹7,300 crore during the same period. That's impressive for a new mobile-based payments system that isn't even a year old.

The huge traction gained by BHIM during the few months since its launch can be explained by various factors.

Modi's personal push by devoting almost an hour on a widely-broadcasted public forum on December 30, 2016 seems to have worked wonders. The Prime Minister's personal touch seems to have had the same effect on BHIM that his unintentional endorsement had in pushing Paytm into popular conscience.

That Modi's magic worked wonders in pushing the adoption of BHIM can be gauged from the fact that on December 31, 2016, a day after he announced the application for smartphone users, almost 43,000 transactions worth ₹1.8 crore were recorded on the platform. In January 2017, a month after the launch,

as many as 1.7 million transactions worth more than ₹350 crore were recorded on the platform.

While Modi's hardsell did give initial momentum to BHIM, its speedy adoption by Indians can also be explained by NITI Aayog's incentive-driven and deadline-oriented strategy. The interim report of the committee of chief ministers released by NITI Aayog this January mentioned cash-back rewards to customers who transact digitally and tax incentives for merchants who adopted these platforms. But the National Payments Corporation of India seems to have wooed even merchants with cash backs.

In a circular dated August 18, the National Payments Corporation of India asked all 55 banks on the BHIM platform to introduce two schemes for customers and merchants. Merchants were given a maximum cash back of ₹1,000 a month if more than 50 unique customers transacted at their establishments using BHIM. To ensure that smaller merchants benefitted from this scheme, banks were asked to reject rewards to large merchants at the time of disbursements. Merchants who could muster a minimum of 20 unique transactions on BHIM were promised smaller sums as rewards. Customers who referred other people to use the BHIM application had ₹25 credited into their bank accounts. A similar sum was also promised to the person who started using BHIM after a successful referral.

As a force multiplier to BHIM's brand placement, National Payments Corporation of India also asked all 55 banks offering UPI services to pre-fix BHIM with their respective applications. Banks could avail these cash incentives only if the BHIM symbol was prefixed to their applications' name.

NITI Aayog had also recommended that National Payments Corporation of India stick to deadlines in expanding and popularising the BHIM ecosystem. By February, the BHIM platform was to be linked to the Aadhaar ecosystem in order to enable even those without smartphones to transact. This eventually set the stage for the formal BHIM-Aadhaar payment system launched by the Prime Minister on April 14. The maximum limit for every transaction on the BHIM-Aadhaar platform was fixed at ₹2,000 and banks were given the option of integrating BHIM and Aadhaar symbols on their applications.

WHILE MODI'S HARDSELL DID GIVE INITIAL MOMENTUM TO BHIM, ITS SPEEDY ADOPTION BY INDIANS CAN ALSO BE EXPLAINED BY THE NITI AAYOG'S INCENTIVE-DRIVEN AND DEADLINE-ORIENTED STRATEGY

Challenges ahead

While BHIM has an early mover advantage, it could face stiff competition from newer entrants. A major challenge to BHIM's prospects would be Google's entry into the UPI payments market with its application named Tez (Fast in Hindi). Tez was launched by Google last month and works on both Android and Apple devices. There are other smaller players in the market, but given Google's technological prowess and dominance of the smartphone software ecosystem, BHIM's toughest competition could well be from the Silicon Valley giant. By the look of it, Google's payments application has 5 million downloads since its launch. How many of these downloads are actually translating into transactions remains unclear. Although its early days for Google in India's financial technology sector, it has been operating a similar business called Google Wallet for American and British customers.

The Modi government could take heart from the phenomenal growth of mobile payment platforms in China, where state intervention hasn't yet allowed Google to dent the dominance of home-bred companies such as WeiXin and WeChat, which control over 90 per cent of the mobile payments market. According to a report published by Paris-based research firm Ipsos this year, the mobile payments market in China has been growing at an annual rate of 195 per cent.

The report notes, "From 2013 to 2016, the number of transactions made through non-banking mobile apps increased from 3.7 billion to more than 97 billion. WeChat Pay has become the main cashless payment method for daily small transactions in China. In the first quarter of 2017, WeiXin and WeChat have a combined monthly active user base of 938 million users, with a year-on-year increase of 23 per cent. WeChat Pay is becoming a part of Chinese people's everyday life."

If the Chinese are anything to go by, BHIM has some way to go in weaning Indians off their love for cash.

REUTERS

AFTERSHOCKS OF NOTE BAN CONTINUE TO JOLT MSME SECTOR

Two million people lost jobs, while labour participation and credit growth saw a sharp decline

SAHIL MAKKAR

A year after demonetisation was announced by Prime Minister Narendra Modi on November 8, the micro small and medium enterprises (MSME) sector is struggling for a revival.

Manufacturers and traders, who earlier complained of a sudden dip in sales, are now finding it difficult to compete with bigger players since the roll-out of the goods and services tax (GST) in July this year.

"Business mai taklif ho rahi hai (we are facing difficulties in doing business). Production has fallen by 30-35 per cent. The GST has added another dimension to the existing problem. It has become difficult for smaller players to stay in business," says Arun Agarwal, senior vice-president of the Federation of Rajasthan Trade & Industry.

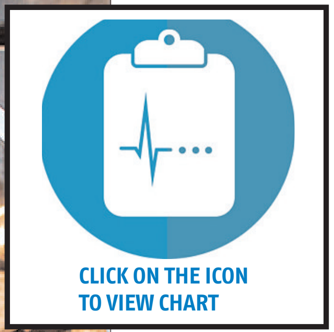
"After demonetisation most industry players opened bank accounts for their workers as mandated by the government. But workers want to be paid in cash," Aggarwal complains.

The lower participation of workers, ostensibly due to fall in production, was also captured by the Centre for Monitoring Indian Economy (CMIE) in its survey. The CMIE's data suggest that the labour participation rate (LPR), meaning the number of people who are either employed or are actively looking for work, has declined substantially after demonetisation. A fall by a single percentage point in the LPR is serious for a country having a large workforce.

The average LPR for January-October last year was 46.9 per cent. It fell to a new low of 44.8 per cent in November, when demonetisation was announced. The average LPR for January-April this year remained at 44.3 per cent, much lower than the 46.9 per cent recorded in the corresponding months a year ago.

Besides a substantive fall in the LPR, around two million people are reported to have lost jobs in the first eight months of this year.

"Around 1.5 million people lost jobs between January and April this year, and another half a million between May



RESERVE BANK OF INDIA POINT TO A WORRYING TREND — DATA SUGGEST THAT THE MSME SECTOR HAS NOT GROWN SINCE DEMONETISATION

and August. So around two million people have lost jobs in the current year. But we can't say for sure whether the job loss was because of demonetisation or any other reason," says Mahesh Vyas, managing director and chief executive officer, CMIE.

The MSME sector is considered to be the biggest employer in the country. According to the Sixth Economic Census (2013), there were 131.29 million persons employed in 58.5 million establishments in the country. Of the 131. 29 million workers (74.83 per cent male and 25.17 per cent female), the maximum (30.3 million) were employed in manufacturing units. It was followed by retail trade, with 27.19 million people and the livestock sector provided employment to another 19.4 million people.

Also, of the 58.5 million establishments, 34.8 million (59.48 per cent) were in rural areas and nearly 23.7 million (40.52 per cent) in urban areas. Most of these units are located in Uttar Pradesh (11.43 per cent), Maharashtra (10.49 per cent), West Bengal (10.10 per cent), Tamil Nadu (8.60 per cent), and Andhra Pradesh (7.25 per cent).

Another set of data from the Reserve Bank of India point to a worrying trend. The data suggest that the MSME sector has not grown after demonetisation. Credit growth has been consistently declining since November last year. For instance, in November last year it was 3.35 per cent against 4.85 per cent in November 2015. Similarly, in December 2016, credit growth declined by 1.73 per cent against 4.46 per cent growth in the corresponding month a year before.

Sudershan Jain, president of the Ludhiana-based Knitwear and Apparel Manufacturers Association, calls demonetisation the biggest culprit behind the decline in sales last year. However, Jain believes that sales will increase in the upcoming season. "The currency is back in circulation and people have adequate cash to meet operational requirements. We believe that sales will pick up this winter," Jain says.

Most manufacturers and retailers Business Standard spoke to say demonetisation has failed to serve its twin purposes of curbing black money and destroying the parallel or informal economy. "It is impossible to end informal trade. The scale of the parallel economy may not be the same as it was before demonetisation, but most businessmen have restored the practice of trading without bills. People used demonetisation as an opportunity to convert their black money into white. They believe that they will circumvent the law by bribing officials," says a Delhi-based factory owner.

Traders say they are worried about the execution of the GST.

Ajay Sahai, director general and chief executive officer of the Federation of Indian Export Organisations, says demonetisation hasn't had much impact on exports because most transactions were through banking channels. "Most have recovered from whatever little impact it had on industry. The problem is delay in refunds under the GST. We believe this will be over in a few months," Sahai says.

WHY KANPUR CAN'T SAVE ITS HIDE FROM NOTE BAN

After November last year, prices fell and the real estate market, which operated mostly in cash, the same as everywhere else, crumbled

Kanpur bears the appearance of a tumbledown, dusty, urban mess with a population bursting at the seams. Seen here is a view of the city's Birhana Road

SUBHAYAN CHAKRABORTY

On November 8 last year, Prime Minister Narendra Modi announced the withdrawal of legal tender status to ₹500 and ₹1,000 currency notes. The move, which drained out 86 per cent of currency in circulation, caused massive economic disruption. While remonetisation subsequently gathered pace, economic activity was disrupted again by the shift to GST. To understand how businesses have fared over the past year, Business Standard spoke to entrepreneurs in Kanpur, Tirupur, Bhiwandi, and Ludhiana.

Just outside Kanpur Central Railway Station, a long line of autorickshaws jostle for space. For the more modern traveller preferring to hail a ride on an app, a group of auto drivers armed with smartphones await.

After starting his vehicle, middle-aged Dinesh Singh tries hard to negotiate through traffic, finally confessing that he has only recently donned the driver's uniform, having been a watchman at a large footwear factory until about four months ago. With two daughters and another child on the way, he says he's lucky to have found work after the factory suddenly laid off workers with only two days' notice, citing lack of funds, following the demonetisation drive.

Now barely able to make the ₹15,000 he earned earlier, he says demonetisation is a good reform which suffered bad implementation but brought about many benefits. "While people have gone back to paying in cash, *notebandi* (demonetisation) has at least introduced more people to apps, through which more and more people are riding nowadays," he says confidently.

WHILE THERE ARE SIGNS OF A MUCH-NEEDED URBAN RENEWAL DOTTING THE SKYLINE OF KANPUR, MOST REMAIN UNFINISHED OR ARE PROGRESSING AT A SNAIL'S PACE

Such is the opinion of the majority of workers, labourers, and traders, who make up the working class of this sprawling industrial city, employing more than 6 per cent of Uttar Pradesh's urban workforce, according to the Sixth Economic Census, 2012-13.

Located less than 100 km from Lucknow, Kanpur bears the appearance of a tumble-down, dusty, urban mess with a population bursting at the seams. While the signs of a much-needed urban renewal such as shopping malls and residential high-rises dotting the skyline, most remain unfinished or are

TROUBLES ARE MORE THAN SKIN-DEEP

LEATHER, GARMENT UNITS MAKE UP BULK OF MANUFACTURING UNITS ACROSS KANPUR...

Type of industries	No. of units
Leather based	2,428
Readymade garments*	1,970
Engineering units	1,211
Agro based	994
Soda water	887

*includes hosiery
Source: MSME Development Institute, Kanpur - Ministry of MSME

...BUT ITS SHARE OF LEATHER EXPORTS CONTINUES TO GO DOWN

Financial Year	Exports from Kanpur (₹ cr)	Total exports (₹ cr)	Share of Kanpur exports# (%)
2014-15	7,160	39,709	18
2015-16	6,430	38,383	17
2016-17	6,142	38,035	16

#in India's exports
Source: Council for Leather Exports, Kanpur

progressing at a snail's pace.

Since the city is so cloistered, land prices in central business districts were much higher than those in other cities in Uttar Pradesh before demonetisation, an officer in the land department of the Municipal Corporation pointed out.

However, after November last year, prices fell and the real estate market, which operated mostly in cash, the same as everywhere else, crumbled.

As project deadlines are pushed back, many shopkeepers of Naveen Market, one of the oldest markets in the city, grow impatient after giving their land for a shopping complex-cum-multi-level car park in the area with the promise of retail space after the property is built.

But with the local councillor brokering a reduction in rent, they say they are ready to wait for another year.

Nearby, the economic casualties of the demonetisation drive and the subsequent goods and services tax (GST) regime, introduced six months later, are visible along the shops nestled in the shadows of tony Mall Road selling leather goods. "With supply from small manufacturers becoming choked, we are forced to source from larger players in the market who dictate prices and have undercut profit margins by half," Sanjeev Shukla, secretary, Small Traders Association, rues.

Kanpur has long been called the leather capital of India. Despite years of losing investment and skilled workers to upcoming hubs such as Chennai, Kolkata, and Noida, the city still has the highest concentration of leather-based manufacturing units in the country and accounts for more than 16 per of all leather goods exports from India, according to the figures of the Kanpur-based Council for Leather Exports.

The industry also supports more than 400,000 people directly, with informal estimates for indirect employment pushing past 1 million. But since November last year, many among the 400 registered tanneries in the eastern suburbs of Jajmau have remained closed for months.

A recent government report shows that more than 60 still remain closed under the dual pressure of demonetisation as well as increasing vigilance by the National Green Tribunal, which has stepped up efforts to reduce effluents flowing into the Ganga. The majority continue to suffer from under-capacity.

"The industry has gone through some adjustment after demonetisation. Firms that focus on exports have not been affected that much. However, since the supply chain was earlier dependent primarily on cash transactions, smaller players have faced difficulties. In the Kanpur zone, we expect revenues in the sector to be hit by up to 20 per cent," said Mukhtarul Amin, chairman of Superhouse Group, a leading leather-manufacturing conglomerate and one of the largest exporters of the country.

However, behind the figures lie raw human stories. Shah Rashid Ali, a karigar (skilled machinist) at one of the units, has gone through nearly six months of unemployment. "Khali pet so jana toh maan lenge, lekin jab kaam karke bhi khali haath ghar lautna padta hai, bohot bura lagta hain (I can go to bed hungry but when you have to return empty-handed even after a hard day of work, it feels very bad)," he says now.

He refers to the fact that with many smaller tanneries still closed and workers in abundance, tannery owners have slashed wages and are allegedly making workers toil for two-three days without payment on condition that they'll be retained for the coming workweek. He says demonetisation helped wipe out illegal cash stashed with local moneylenders in his village near Unnao but also points out that farmers facing distress have had to sell good farmland at throwaway rates.

The hosiery industry — the city's second largest in terms of the number of units — hasn't fared any better. Unlike leather, while many companies have adopted vertically aligned operations, thereby reducing risks arising out of demonetisation, the GST has been the principal bane here. "We have a lot of customers in non-urban areas who are still confused about the rules. They have stopped buying from organised players," said Balram Narula, managing director of Jet Knitwear.

Traders had been petitioning the government authorities to allow land to expand the hosiery manufacturing cluster in the city's Dadanagar locality. The Kanpur hosiery market is about ₹600 crore, which is bound to dip by more than 20 per cent, Narula says.

However, one Kanpuria has made it his mission to vote out the Bharatiya Janata Party at the Centre, come 2019. Silver-haired Raghunandan Pandey, a veteran porter of 26 years at the railway station, seethes with anger while eyeing younger ones running towards potential patrons. These new entrants into his profession were all labour hands at small garages near the station and have lost their jobs over the last year and are now practically crashing the established rates for luggage hauling.

Asked whether demonetisation is responsible for this predicament, he says he doesn't care as long as they go back wherever they came from.

This piece appeared on www.business-standard.com on November 2, 2017

TIRUPUR KNITWEAR INDUSTRY FRAYS AT THE SEAMS

The 1,200-odd units in Tirupur's main market and other job works centres were doing a business of ₹15,000 cr before Nov 8. Today, not even 40% of that business is left

The roads are deserted and Khaderpettai Market looks like a ghost town. Shopowners gather to talk their time away because customers are very thin on the ground

T E NARASIMHAN

A year ago, S Venkatesh was running a job works unit and was employing around 10 people. Today, he works as supervisor in a large garment unit in the knitwear hub of Tirupur. He is one of the hundreds of workers who had turned entrepreneurs, but had to again fall back on doing jobs as they decided to close down their factories, not being able to withstand the pressure of demonetisation, followed by the goods and services tax (GST).

The situation is not different in Khaderpettai Market, which sells clothes that have been rejected in the export market in Tirupur. These are branded cotton clothes made for exports, but have not made the international cut and ended up in the domestic market.

The more than 1,200 units in this market and other job works units were doing a business of around Rs 15,000 crore before demonetisation. Today, they say not even 40 per cent of the business is happening.

Tirupur's textile industry

Tirupur, a tiny town 450 km south of Chennai, is the hub of the knitwear industry. It houses exporters; merchant exporters, who take contracts from exporters; and domestic suppliers.

Exports are a Rs 26,000-crore industry and primarily cashless. But demonetisation has affected business because they have to give cash-based subcontracts to merchant exporters for job works such as knitting, buttoning, small servicing, printing, and packing. Merchant exporters themselves are small units with a workforce, which is paid in cash. The Tirupur Exporters' Association estimates the turnover of domestic units at Rs 7,000 crore from accounted transactions and another Rs 7,000 crore from cash transactions, which are largely

THE WARP AND WEFT OF TIRUPUR'S FABRIC

Turnover: ₹41,000 crore (Including exports: ₹26,000 crore; domestic: ₹15,000 crore)

No. of people employed: 600,000 directly

Specialisation: Knitwear

Vision: ₹1 lakh crore by 2020

unaccounted. On the other hand, unorganised units run on just cash and are estimated to have a turnover of Rs 15,000 crore.

A year before — and today

In October last year, a month before demonetisation was announced, Tirupur was busy executing festival orders. The narrow roads of Khaderpettai were busy with customers. Today, the roads are deserted and the place looks like a ghost town. Shopowners gather to talk their time away because customers are very thin on the ground.

A Mohamed Imayil, owner of Limra Garments, is one such shopowner. He says the impact of demonetisation and the GST continues. A majority of the customers at this market are roadside shopowners from across the country.

He says that business is down by 60 per cent and since he is not in a position to pay salaries, he has reduced the number of employees to four from 15.

M G Kumar, owner of SKM Tex and one of the officer-bearers of the Khadarpet Association, agrees with Imayil and added that more than 300 shops have closed down in the past six months.

K S Babuji, general secretary, South India Collar Shirts and Inner Wear Small Scale Manufacturers Association (SISMA), says of the 2,000 units — all SISMA members — 30-40 per cent have closed down. They were giving jobs to 60,000-80,000 people, directly and indirectly.

The Tirupur cluster alone directly employs more than 600,000 people. What is interesting is that no one here is against demonetisation or the GST. In fact, people like Babuji campaigned for the Bharatiya Janata Party so that Prime Minister Narendra Modi could replicate his success in Gujarat all over India.

All say the issue is implementation. Money rotation continues to be a matter of concern among traders. Besides, there is fear among customers who don't want to spend, says A Sundaram of Jayavel Textiles. Compared to last Diwali, the order flow was down by 30 per cent and for the first time, the children-wear segment saw a dip of 25 per cent.

Tirupur was badly affected because it is largely a cash-based economy. The caps on daily banking transactions also affected the system, said S Rajendran, owner of a unit here. If workers are not paid their wages in time, they do not return to work the next week. Babuji notes, for example, workers need to be paid bonuses and they, and their union, have insisted that they be paid in cash, though the rules do not allow that.

S Muruganandam, who works at Imayil's factory, says his owner cannot pay the entire salary because the order flow has dropped drastically.

The farmer-turned-daily worker says he does not have a choice but to continue as he will not able to pursue any other jobs, especially agriculture. Like him many of the workers are paid or supported by owners to take care of the basic necessities. If this trend continues, the only option for them is to move from the city to places like Chennai or other cities.

Already many of them have moved to the construction industry in the neighbouring towns and districts. Besides, as most of the workers are migrant workers, opening accounts for them is an issue.

What small businesses want

A four percentage point reduction in the GST rate, ease of doing business, and making bank credit available will put the industry here back on track, say small business owners. It is the source of livelihood for more than 800,000 people in Tamil Nadu and neighbouring states, including 100,000 migrant workers from the North-East.

This piece appeared on www.business-standard.com on November 3, 2017

ANGER AT GST, NOTE BAN SIMMERS IN LUDHIANA

People in business question the manner of execution of demonetisation and ask why there was not a bigger interval between the two

PHOTO: ARUP ROYCHOUDHURY

Workers at a garment manufacturing facility in Ludhiana's Focal Point industrial area

ARUP ROYCHOUDHURY

Winter is coming to smoggy, polluted Ludhiana, the centre for hosiery, garments, and textiles. October-February is when business booms in this city. But if you ask traders and manufacturers, this time could be different. Business could be slower. That is because this winter will be the first one after demonetisation, and the goods and service tax (GST).

Business Standard spoke to a number of people who form a vital part of the textile and hosiery supply chain. The industry, which has traditionally been cash-intensive, has taken a massive hit and demand is still not close to pre-demonetisation levels. There have been lay-offs, businesses are running at wafer-thin margins, there is a shortage of working capital, and businesses are downsizing.

Industry voice

Harinder Pal Singh sits in a glass cabin perched above his factory floor in an industrial area on the outskirts of the city. His company, Poonam Textiles, makes sweatshirts and t-shirts, which it sells to wholesalers, retailers, as well as through six self-branded stores. When I walked into his office, he was downloading from whatsapp a newsclip featuring BJP leader Subramanian Swamy, on his ipad.

Singh's jovial demeanour turned serious when he was asked about the impact of demonetisation and the GST on the garments and textile business. "My turnover, in 2015-16, was around ₹11 crore. In 2016-17, after demonetisation, it went down to around ₹8 crore. We have recovered a little, but this winter may not be as good. For smaller businesses, it is even worse."

Singh has two stores in Ludhiana, one in Dehradun, and three in Delhi. "I am exiting the Delhi business. There is just no demand. All three stores will be shut down by the end of November. We wanted to expand our business to boost margins by cutting out the suppliers and middlemen. That is why we opened our own stores.

After the note ban and GST, if you ask me if I would take that decision, I will say no. Expansion is impossible now," he says.

As we speak, a worker walks in from the factory floor. "Sir, *koi kaam nahi hai* (there is no work)". "*Koi gal nahi beta. Do din ruk jaa, naya* order *aa sakta hai* (no worries, son. Wait a few days, we may get a new order)," Singh replies. He admits to me that for an industry dependent on cash, the note ban has hit hard. "See, a customer will pay usually for clothes or garments in cash. That cash goes up the chain from the retailer to the supplier/wholesaler to the manufacturer. When cash dries up, the supply chain gets crippled. The effects are still showing."

Singh maintains that even before demonetisation, most of his transactions were through cheques or online banking. But retailers and suppliers have no hesitation in admitting that because of heavy cash usage they used to maintain two books, one of which was for the taxman's eyes. Of course, after admitting that, they seldom want to come on record.

"In the past retailers would not always maintain proper records, or present bills. After the note ban and GST, the good thing is that has changed. People have had to get their GST numbers. But then there are the very small businesses, which don't come under the GST. Not all of them have PAN numbers either. A number of them are out of work already since nobody wants to deal with them," says a retailer.

"October-February is also the wedding season. So far this year, the demand is just not picking up. The labour force here is migrants, from UP and Bihar. As such, there is a shortage. If sales remain muted, I may have to downsize," the retailer said.

Note ban at work

According to industry sources, India's garments industry is ₹25,000-30,000 crore. Ten-fifteen per cent of that comes from woollen products, and 90 per cent of that is based out of Ludhiana. According to the latest data, dated 2011-12 and available on the website of the ministry of micro, small and medium enterprises, the MSME textile and apparel industry in Ludhiana district hires 106,000 people. Businesses say there have been job losses. But queries to multiple industry bodies have elicited no response to how many people were laid off exactly.

In this flashy, wealthy city, where every second car is modified with after-market parts (you will even find humble Maruti Altos running on faux-chrome alloy wheels and fat tyres), people admit that there was a lot of unaccounted wealth. Harinder Singh says that in the initial days after Prime Minister Narendra Modi announced demonetisation on November 8, there was a glut of cash as people were placing orders and paying employees three-four months in advance.

This is echoed by brothers Rajinder and Ashok Uppal, who run Punjab Metal Fabricators, which makes components for sewing machines. "There was so much cash. Even clients who never paid on time promptly paid in advance. But after that came the shortage as banks just could not distribute money in an organised manner. We don't doubt the government's intentions regarding the note ban and GST. Our problem lies with the very shoddy implementation," said Rajinder Uppal.

INDUSTRY STRENGTH

Textiles and wearing apparel industry (For 2011-12)

No. of MSME units	7,883
People employed	106,191
Investment (₹ crore)	524.5
Production (₹ crore)	7,698

Source: dcmsme.gov.in

"Our business was 60-70 per cent through cheques or online banking and 20-30 per cent cash before the note ban. The cash component has reduced now. The biggest problem we now face is the lack of clarity regarding the GST. Sewing machines are in the 12 per cent bracket. But there is confusion regarding the components. Some say 12 per cent, some say 18 per cent. GST officials at the local level are not of much help. We have made representations even in Delhi, but not much has come of it," says Ashok Uppal.

He says that while some industries have bounced back, like sewing machine and bicycle components, the city's biggest sector, textiles, will continue to suffer. The government should have had some gap between implementing the note ban and GST. They happened just eight months apart. The view is that before the businesses could fully recover from one, the other happened," says Rajinder Uppal.

The complaints

Another problem, this one GST-specific, which businesses face is that chartered accountants and advocates, who understand the intricacies of the new, nationwide tax, are in short supply. Accountants are charging more, and that eats into the margins. "We have hired another person just to deal with GST issues. There are multiple filings to be done and we are still trying to understand the impact on our business," said Parash Jain. His company Hem Knitwears, with a turnover of ₹50 crore, supplies yarn to manufacturers across the country.

"For us, it is a margin game. And since the note ban and GST, margins have been squeezed further. I understand why the GST was necessary but I am not so convinced about demonetisation. First, the government made a mistake by printing the ₹2,000 note. I feel there are other ways to go after those with black money. The 75 per cent amnesty scheme could be done even without withdrawing notes from circulation," Jain said.

The Pradhan Mantri Garib Kalyan Yojana was launched by the Centre a month after demonetisation. It provided an opportunity to declare unaccounted wealth and black money in a confidential manner and avoid prosecution after paying a tax, surcharge, and penalty, which added up to 50 per cent on undisclosed income. An additional 25 per cent of the wealth will be invested by the government and will be refunded after four years, without any interest.

There is certainly a growing murmur against the Centre. "The note ban and GST have made even die-hard supporters of Modi question the government's abilities. I still believe his heart is in the right place," says Harinder Singh. "However, I believe that had doctor *sahib* (former Prime Minister Manmohan Singh) ever implemented such schemes, he would have ensured things went smoothly. He has the economic expertise and would have done things more intelligently."

"You require expertise to ensure people don't suffer. Small businessmen come to Ludhiana from across North India to buy clothes. What about them? You can be a good person. But that does not mean I would allow you to do heart surgery just on that basis," Singh says.

PHOTOS: SUBRATA MAJUMDER

Empty bylanes of Burrabazar, which are otherwise busy ahead of the wedding season

NOTE BAN, GST HAUNT KOLKATA'S BURRABAZAR

Amid low demand and margins, traders at one of Asia's largest wholesale markets are mulling shutting shop

NAMRATA ACHARYA

Almost a year since the note ban, Kolkata's Burrabazar, one of the largest wholesale markets in Asia, is still reeling from its aftershocks.

Prime Minister Narendra Modi had announced the demonetisation of old ₹500 and ₹1,000 notes on November 8 last year. But, even now, sales at Burrabazar are yet to recover to half the levels at which they were before.

Immediately after demonetisation, which sucked out 86 per cent of the cash in circulation, business had fallen by 50-90 per cent in different parts of Burrabazar. The wholesale market comprises 25 submarkets or katras that supply goods to much of east India.

Since then, the market has not had an opportunity to recover. The roll-out of the goods and services tax (GST) on July 1 this year was another major disruption.

With sales falling to almost nil, some wholesalers are planning to down shutters.

"Retailers are not buying from us and supplies from other states have come

YOGESH KUMAR SONTHALIA, A TEXTILES MERCHANT IN BURRABAZAAR, SAID HE HAD ATTEMPTED TO ROUTE TRANSACTIONS THROUGH PAYTM SOON AFTER DEMONETISATION LAST YEAR. HOWEVER, HIS BUYERS HAVE BEEN REFUSING TO USE PAYTM, WITH TRANSACTIONS THROUGH IT REMAINING CLOSE TO NIL

"IF I KEEP AN ACCOUNTANT, I WOULD HAVE TO SPEND AT LEAST ₹25,000 AS MONTHLY SALARY. EVEN FOR SMALL THINGS SUCH DEPOSITING CASH IN BANKS, TRADERS ARE BEING HARASSED. ON TOP OF THAT, THERE IS NO DEMAND [FOR GOODS]"

GOVIND AGARWAL
Owner of a wholesale spice shop in Burrabazar since 1978

down by more than 50 per cent in the last two months. People are scared of the huge amount of paper work. There is a sense of terror among retailers," said Biswajit Saha, president, Rajakatra Byabsayi Samiti.

At Posta Bazar, another sub-mart for perishable commodities, turnover has come down by at least 40 per cent in the last two months, said Shyam Sundar Agarwal, chairman, Posta Bazar Merchants' Association. It has nearly 450 members.

"Till now, business was carried out informally. But now, all of a sudden, some of the small traders are required to use computers for even a minor transaction. Moreover, with cash transactions not allowed above ₹10,000, traders are having problems in even paying transporters and porters, who only want cash, as they are daily wage earners," Agarwal added. Recently, members of the Posta Bazar Merchants' Association met Finance Minister Arun Jaitley to discuss the problems they were facing.

Other merchants in the area corroborated the claims of business slowdown.

Govind Agarwal has been running a wholesale spice shop in Burrabazar since 1978. He claimed he had never experienced such a slowdown in his life.

"If I keep an accountant, I would have to spend at least ₹25,000 as monthly salary. Even for small things such depositing cash in banks, traders are being harassed. On top of that, there is no demand [for goods]," said Agarwal.

The worst hit are the small traders, who don't have permanent shops but operate out of makeshift structures or carts.

Mohammad Abbas, a toy seller, used to earn about ₹250-300 per day till October last year. Now, his daily earnings have come down to ₹70 a day.

"Due to lack of supply of Chinese toys, stocks are down by 75 per cent," he said. "Electric toys attract 18 per cent GST against the earlier 12 per cent VAT (value-added tax). Other toys attract 12 per cent GST against 5 per cent VAT. Prices of various plastic products have increased by about 25-30 per cent due to the GST, forcing shopkeepers to raise prices. But demand remains low. So sales have almost stopped."

Another trader, Mohammad Heera deals in tarpaulin. His daily sales have fallen from ₹2,000-2,500 per day to less than ₹500-1,000. Prices per unit have gone up by ₹200.

Bag seller Mohammad Mustaq has to now wait till 1 pm to get his first customers. Demand for his goods has come down by 50 per cent.

Digitisation was one of the motives for demonetisation. Burrabazar has, however, has firmly resisted a move away from cash. In the past year, not even 5 per cent of the business had moved to digital means, said market insiders.

Yogesh Kumar Sonthalia, a textiles merchant in Burrabazaar, said he had attempted to route transactions through Paytm soon after demonetisation last year. However, his buyers have been refusing to use Paytm, with transactions through it remaining close to nil. Meanwhile, sales have crashed by 30-40 per cent in the last two months due to GST.

Another cloth merchant, Navin Harlalka, said his margins fell by half in the last one year, from about 10-15 per cent to 5-7 per cent at present. Like most others at Burrabazar, he is waiting for normalcy and praying that there are no more disruptions.

THE BIGGEST SHOCKER INDIANS GOT IN A DECADE

Ordinary people spent days standing in queues; for some, a friendly banker meant a shorter wait; the privileged ones managed things from the comfort of their homes or offices

AMBAREESH BALIGA

Demonetisation, unleashed on Indian citizens on November 8, 2016, will probably go down as the biggest shocker for them in a decade. As the dramatic late-evening announcement by Prime Minister Narendra Modi started sinking in, the bank and bank managers suddenly became the most important entities in our lives. The ordinary mortals spent the next few days standing in queues, while for some, a friendly banker meant a shorter wait. The privileged ones managed everything from the comfort of their homes or offices. However, this gave rise to a new opportunity that was immediately encashed by the so-called "consultants" and "brokers" for a fee. For the next couple of weeks, all discussions revolved around demonetisation.

Before the note ban, India's GDP was growing at more than 7 per cent and it was expected that growth would move up in the third year of Narendra Modi's government, as that is when all the initial work starts to yield results. Then, suddenly, on that fateful day, Prime Minister Modi declared this was a war against black money, corruption and fake currency. The PR machinery successfully convinced people that this pain was a "sacrifice" to catch the black money hoarders. However, over the next seven weeks, with the pressure building up amid public angst, the narrative shifted to cashless economy and formalising the grey economy, thus increasing the tax base. Initially, for four weeks, we were fed the demonetised cash return data to prove the success of the scheme, but when the figures crossed 80 per cent of the demonetised currency, the data sharing was stopped abruptly on December 13.

There is no doubt that obscene amounts of black money were generated in the past few decades, especially the last one. The question remains whether most of that was lying in cash in India? Reports suggest that it was mostly transferred abroad or converted into assets, mostly properties and gold. I wouldn't discount the fact that some of it has been converted into "white" via the stock market utilising the long-term capital gains benefits. So,

the big black money seems to be parked safely and that which was left in the system might have been loose change.

Black money is generated primarily via two routes. First, profits earned in ethical businesses but taxes wilfully avoided. And second, earnings out of banned activities like terrorism, underworld dealings, extortions, corruption, etc. Though the colour is the same, the solution is not. It seems the government erred on this point and that led to catastrophic consequences, albeit for a month. The collateral damage continues to this day. The bitter truth is that a significant part of India's small and medium enterprises fall in the first category. More importantly, they provide employment to a large part of the population.

We come back to the question whether looking at the year gone past, did demonetisation achieve the objective it was meant to?

Today, the currency in circulation is back at nearly 90 per cent of the October 2016 levels. Digital transactions shot up immediately after demonetisation as 86 per cent of the currency was sucked out. However, the pace slowed down as cash returned to the system. Demonetisation forced many non-digital ones to convert but failed to lead to a tectonic shift the government was expecting.

And has corruption reduced drastically post Demonetisation?

It took the Reserve Bank more than eight months to confirm that nearly 99 per cent of the currency (or is it actually more than 100 per cent) was deposited with banks. How the government will be able to prove the quantum of black money among these deposits is a subject of probe and litigation which might go on for the next few years. The fake currency fear also seemed unfounded as only about 762,000 pieces of fake currency amounting to less than ₹20 crore were detected in 2016-17. This is merely 20 per cent higher than the previous year, proving the demonetisation exercise did not add a huge number. Thus the initial reasons for demonetisation go out of the window. Coming to the argument of shifting from grey economy to formal economy, I would ask whether it needed such a huge blow, especially when GST was in the works. There are times when you need to push through a change, but if that puts very livelihoods of a large number of people at peril, you should avoid that path.

> **IT TOOK RESERVE BANK OF INDIA MORE THAN 8 MONTHS TO CONFIRM THAT NEARLY 99% OF THE CURRENCY (OR IS IT ACTUALLY MORE THAN 100%) WAS DEPOSITED WITH BANKS**

The small & medium enterprises were badly hit as the cash crunch eroded their working capital and the overall slowdown which ensued resulted in lower order flows. There are reports that many have already shut shop and the trend would continue due to the GST disruption. This brings to the fore the question of employment since this segment is a huge employment generator both in the formal and informal sectors. The workers might be left high and dry, while employers' capital might find its way into the stock market for more profitable deployment. The money (whether black or white) invested in an economic activity, generating revenues and providing employment, was now deployed in speculative activity.

Demonetisation also threw up a few beneficiaries. It resulted in unexpected gains for a section of the population that helped convert the old demonetised notes into new ones. This resulted in partial distribution of wealth. The money stashed away earlier was now transferred to bank accounts. Many families would have realised that they had more money than they had displayed earlier. After a month or two of shock, part of this money flowed into consumer buying. Again, the question is whether such buying can sustain without fresh generation.

The biggest beneficiary of the demonetisation move, however, was the stock market. Lower fixed deposit rates, a depressed real estate market and lack of other investment avenues resulted in the TINA (there is no alternative) factor playing out. Huge liquidity on the one side and a performing stock markets on the other, resulted in relentless flows, playing out a vicious cycle. Even the retail liquidity which found its way into the stock market, whether directly or via mutual funds, are finally being deployed for speculation (whether we call it short-term trading or long-term investment). How much of this money is flowing into the creation of revenue-generating assets for the economy? Even the IPO route nowadays is mostly used to liquidate investments of the government, promoters and private equity investors. I wonder how an economy can grow without asset creation at the ground level along with weak employment generation.

Demonetisation is one such decision that once set in motion cannot be reversed, but it could be tinkered with. This tinkering resulted in about 66 notifications in a matter of seven weeks, which could be a record in itself.

If the clock were to be turned back, I am sure, with the benefit of hindsight, Modi would have given a miss to the demonetisation idea (if it was really meant for the purpose of eradicating black money, etc, as publicly announced) and concentrated on GST to achieve his goals of a largely formal economy. It would have averted a forced slowdown, the direct costs of demonetisation and deaths of many innocent citizens.

The author is an independent market analyst. Views expressed are personal

A TALE OF CHANGING GOAL POSTS AND LIMITED IMPACT

The RBI has revealed that almost all the money that was withdrawn has come back into the system, which means that households still prefer to hold cash

MADAN SABNAVIS

Demonetisation was an attempt to address issues like black money, terror funding and counterfeit currency. Somewhere along the way the goal post changed to digitising the economy to leave a better audit trail. Even as it caused a lot of physical inconvenience to the public, which can be the cost of such a bold programme, the economic impact is still uncertain.

The RBI has revealed that almost all the money that was withdrawn has come back into the system, which means that households still prefer to hold cash. The government has revealed that the number of taxpayers has increased, though the extra income that could be earned through taxation is still a matter of conjecture. As the amount collected through the declaration schemes has not yet been disclosed, the gains from the macro perspective would be futuristic and not significant in the short run. However, this precise impact might still be hard to separate, given the turbulence also being caused by the Goods & Services Tax (GST).

It is also debatable as to what could be the impact on GDP growth as data are unavailable and subject to substantial revisions by the CSO. But going by the logic that growth in a not-so-good year 2015-16 was 8 per cent, and that in 2016-17 was 7.1% despite all economic conditions being very good — from rains to demand — a thumb rule could be that at least 1 per cent decline in GDP could be attributed to demonetisation as the period involved five months.

Non-availability of cash did affect the SME segment in particular as transactions here are cash-based on both ends which restricted activity. While agri markets too were affected, normalcy was restored in due course of time. However, for SMEs, given the severity of the problem and the resultant unemployment, the impact was more serious. To top it all, GST later put further pressure on their operations, and while the government has been trying to address these issues, it could take another three-four quarters before normalcy is reached.

The important question is whether or not we have gone past the worst of the demonetisation impact. Based on the presentations made by several companies dealing with consumer-related products — consumer goods, automobile, real estate — the shadow of disappearing currency had left its imprint till June 2017.

The macro numbers that are available on different sectors, such as industrial growth, including core sector and critical sectors, do indicate that the worst is over from the point of view of demonetisation and the problems now are more on account of adjusting to the GST regime. This can also be attributed to the remarkable manner in which the RBI has brought back the currency required within a span of six months or so to eschew any new challenges on the availability of currency.

The significant increase in digital payments can be a plus point scored by demonetisation, though at some point of time there would be a need for a reconciliation of the cost involved in such a system — at the end of the day someone has to bear it. But it would still be premature to conclude that digital payments have substituted the use of cash. It is more likely that the two are complementary.

The author is chief economist, CARE Ratings. Views expressed are personal

STRONGEST DRIVERS OF ECONOMY WERE THE WORST HIT

Consumption and services, the strongest drivers of pre-demonetisation growth, weakened significantly after December 2016, as reflected in the steady de-growth of consumer durables until recently

RUPA REGE NITSURE

This piece on demonetisation impact is likely to be criticised as the logical fallacy – Post Hoc Ergo Propter Hoc, which means "after this, therefore because of this". This is because even before "demonetisation" was launched on November 9 last year, India was facing several macro headwinds and uncertainties (both domestic and global).

Domestically, some risks to growth had emerged due to the lingering effect of three subdued monsoons (2013-15), continued balance-sheet stresses for large corporates and banks and the large-scale redemption of NRI deposits. Globally, developments like Brexit, monetary policy normalisation and election fever in the US had increased pressure on the rupee and rupee liquidity. Yet, there were a few bright spots. Monsoon in 2016 was near normal, investment sentiment was up marginally, though restricted to consumer goods, automobile, roads and renewables. Micro & small units from manufacturing had started doing better in terms of profitability, and services' growth held firm in double digits for many quarters before demonetisation was effected.

And, these were precisely the sectors that suffered a direct blow from demonetisation. Activities in agriculture, rural belts and unorganised segments suffered the most due to their high dependence on cash transactions. Mandi prices of food grains, especially pulses (a proxy for farmers' income) crashed across the nation and the downtrend continues even today. This gave rise to farmers' protests and demand for debt waivers, with dreadful consequences for states' fiscal positions. Already, five states – Maharashtra, UP, Punjab, Karnataka and Rajasthan – have announced loan waivers in 2017-18 and reports say a few more states are considering such loan waivers.

Consumption and services that were the strongest drivers of pre-demonetisation growth weakened significantly after December 2016, as reflected in the steady de-growth of consumer durables until recently. Within services, trade, real estate, hotels & restaurants, construction and transport were particularly hard hit. Investment sentiment, already fragile, further deteriorated, as shown in the sustained de-growth of capital goods' production and the collapse of average bank credit growth to commercial sector from 9.9% in January-October, 2016, to 5.6% in the period from November 2016 to September 2017. Several micro and small companies went out of business as they could not get working capital. This is amply captured in quarterly corporate earnings. Also, nearly 5 million jobs were lost after demonetisation, according to some estimates. Banks' balance sheets (saddled with large corporate stresses) suffered additional stresses coming from retail and MSME sectors after demonetisation.

The RBI had to manage excess liquidity after demonetisation using conventional and unconventional measures which took a heavy toll on its payout to the government. While some "migration" happened from cash to digital payments in the first few months after the demonetisation move, there was a decline in electronic payments subsequently once sufficient currency was back in circulation. Empirical research shows migration from cash to digital payments is a very slow process and directly linked to the nation's state of development.

As stated by the government's Economic Survey, true losses from demonetisation can never be measured accurately, as informal sectors (that witnessed de-growth) are not captured adequately in our GDP measurement.

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WE ARE PLAYING FOR THE FUTURE NOT PAST

Demonetisation and GST did have an impact, to an extent. However, economists and markets had already expected a slowdown

RAHUL JAIN

The year 2016-17 will be remembered in India's history for major structural reforms. In November 2016, the Government decided to ban high-value currency notes of ₹500 and 1,000 denominations. Eight months later, Goods and Services Tax (GST), the unified and simplified indirect tax regime, was implemented nationally. Nearly a year since demonetisation and the subsequent implementation of GST, the dent on the economy has been substantial.

According to the International Monetary Fund (IMF) estimates, growth will climb back to 8 per cent over the medium term, once again restoring India as the fastest-growing economy globally.

Economic indicators signal a strong recovery

The data that have flowed over the past few weeks signal towards a revival in growth. High-frequency indicators for consumption, such as two-wheelers and passenger vehicle sales (+14 per cent), fuel consumption (+10 per cent), festive sales for e-commerce portals (+15 per cent), and other macro indicators like exports growth (+25 per cent) and industrial production (+4.6 per cent) paint an optimistic picture. If one looks at the past two quarters in totality, the averages signal a steady pace of recovery adjusted for the short-term impact of the reforms.

Shot in the arm to the banking system

Inflation in September remained unchanged at 3.28 per cent, with food inflation pulling the inflation down. However, the probability of another rate cut seems weak. Of the total capital infusion, ₹1.35 lakh crore is supposed to come via recapitalisation bonds and ₹76,000 crore via market loans and budgetary support. Total stressed assets of state-run banks would amount to around ₹8 lakh crore. Of this, provisioning has been down to the tune of ₹4.55 lakh crore. Taking a 50 per cent haircut, government banks' un-provisioned stress would amount to around ₹1.72 lakh crore. Thus, the amount announced seems adequate.

FOCUS WOULD RATHER BE ON THE TRANSMISSION OF LOWER INTEREST RATES RATHER THAN FURTHER CUTS. BANKS HAVE THUS FAR BEEN RELUCTANT TO PARE LENDING RATES ON ACCOUNT OF STRESSED ASSETS

In this scenario, the focus would rather be on the transmission of lower interest rates rather than further cuts. Banks have thus far been reluctant to pare lending rates on account of stressed assets. Much to the discontent of the Reserve Bank of India (RBI), banks have not kept pace with the transmission of rate cuts passed on to borrowers. The marginal cost of funds-based lending rate (MCLR), which came into effect in April 2016 for effective implementation of rate cuts, has only been lowered by 0.23 per cent over the past year.

Exports surging, trade and current account deficits under control

Exports surged to a nine-month high, rising 26 per cent (y-o-y) in September. On a 3-month moving average basis (3MMA), exports grew by 13 per cent (y-o-y). Global Tailwinds like improving global PMI along with smoothening of GST-led disruptions aided recovery in exports. Engineering goods continue to drive export growth. Imports have also slowed down, mainly due to lower gold imports. Gold imports

declined by 5 per cent in September, against a rise of 68 per cent in the previous month.

Attacking the GST loophole by imposing a ban on gold imports from countries like South Korea and Sri Lanka seems to have borne fruit. The trade deficit narrowed to $9 billion in September from $11.7 billion in August. Going ahead, we expect trade and current account deficits to both remain in check for FY18. We estimate current account deficit to be around 1.5 per cent of GDP for FY18.

Ambitious projects announced

The government announced the biggest road construction programme in India's history to create 84,000 km of roads over the next five years, with a total investment of ₹6, 92,000 crore. After the National Highway Development Programme (NHDP) planned during the previous NDA government, this is the biggest road construction activity planned in India with a clear road map for execution and financing.

Importantly, a clear road map has also been given out for financing the the overall capital requirement. Of the ₹6.92 lakh crore, ₹2.09 lakh crore would be market borrowings, ₹1.06 lakh crore is expected to come from private participation, ₹2.19 lakh crore will be funded through the Central Road Fund, ₹59,000 crore will be budgetary support and ₹34,000 is expected to come from monetisation of existing road assets under the toll-operate-transfer (ToT) model.

GOVERNMENT ANNOUNCED THE BIGGEST ROAD CONSTRUCTION PROGRAMME IN INDIA'S HISTORY TO CREATE 84,000 KM OF ROADS OVER THE NEXT FIVE YEARS

Globally, industrial activity and economic growth have continued to rise at a robust pace. Geo-political risks, though, continue to remain elevated. They are high-intensity but less probable events. However, such events cannot be predicted.

Market and earnings outlook

Indian equity markets seem heading towards a stellar quarterly performance in Q2 FY18, mainly driven by restocking after GST-led disruption and low base for state-run banks. At the onset of the result season, we had estimated a 13 per cent rise in earnings growth for the Nifty. Going by the results that have been released so far, our estimates look realistic. The Indian macro scenario looks stronger than ever, with low inflation, buoyant exports and fiscal stimulus. Loose monetary and fiscal policy augur well with economic growth.

We continue to remain bullish on the Nifty, as there are long-term growth levers. Road construction, financials, consumption and commodities continue to be our top sectors. As earnings growth pick up in the remaining quarters, the target of 11,100 by March 2018 seems achievable. With an earnings-per-share growth estimate of ₹515 for FY18, the Nifty currently is trading at 19x. Looking at forward guidance and expected growth trajectory, it looks like the rally will continue.

Conclusion

Demonetisation and GST did have an impact, to an extent. However, economists and markets had already expected a slowdown. So, as investors we should be aware about what we are playing. We are playing for the future not the past.

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